

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:PSI:4\PLR-145477-01

Date:

JUNE 24, 2002

Legend:

Decedent	=
State	=
County	=
Department	=
Date 1	=
Date 2	=
State Statute 1	=
State Statute 2	=
State Statute 3	=
Sister	=
Settlor	=
Trust	=

\$w	=
\$x	=
\$y	=
\$z	=

Dear :

This letter is in response to your authorized representative's letter dated August 23, 2001. Your representative requests a ruling that the value of the assets held in Trust on the date of Decedent's death is includible in the Decedent gross estate. Accordingly, pursuant to §1014, the basis of each asset held in Trust is increased to its fair market value as of Decedent's date of death.

Facts:

According to the facts submitted, Decedent, a United States citizen, died on Date 2, a resident of County, State. At the time of his death, Decedent resided in a long-term care facility in County. Department (the County Department of Social Services) paid the expenses of Decedent's care under the Federal Medical Assistance (Medicaid) program.

Several years prior to his death, Decedent was injured in a vehicular accident that resulted in severe, permanently disabling injuries. A lawsuit was brought against a hospital relating to the care that Decedent received at the time of the accident. The case was settled on Date 1. Under the terms of the settlement agreement, Decedent received a lump sum payment of \$x, after reduction for attorney fees and expenses. Pursuant to the court order approving the settlement, the funds were paid to Decedent's sister, Sister, as the trustee of Trust, an irrevocable "supplemental needs trust" established in accordance with State Statue 1 and 2, to receive the settlement proceeds and to administer the proceeds for Decedent's benefit. Settlor, as guardian-ad-litem for Decedent, established Trust.

Article 1.3 of Trust provides that because of the nature of the disability of the Decedent, at the time of execution of the trust, it is settlor's intent that the special provisions of the trust be strictly enforced. It is the settlor's intent that the Decedent shall receive all government entitlements that the Decedent would otherwise be entitled to but for distributions under the terms of Trust. Settlor intends that Trust conform to State Statute 1 and State Statute 2, and 42 U.S.C. §1396p (d)(4)(A).

Article 2.1 of Trust provides that the income of Trust is to be distributed for the benefit of Decedent, but only in accordance with the strict limitations of Trust. The income is to be distributed for the "special needs" of the Decedent that are not provided for by government entitlements, and as defined by Trust. It is intended that any distribution be made with a recognition of the special needs of the Decedent who because of the nature of his disability, will be dependent on government entitlements for life.

Article 2.2 provides that except as otherwise provided in Trust, there is to be no invasion of principal except in the trustee's discretion and pursuant to order of the court which has jurisdiction over the guardian of the Decedent.

Trustee has the right to invade principal up to the sum of \$y annually for any supplemental needs. Such use of principal may be made to supply services and items of need not otherwise provided through government entitlements and consistent with the use of funds as provided in Trust. It is the intention of Settlor to supplement, rather than supplant, government entitlements. Notwithstanding, the trustee shall have the discretion to invade principal for the exclusive purpose of obtaining transportation for the Decedent. The type of transportation will be for example, the purchase of a motor vehicle appropriate to the special needs of the Decedent.

Under Article 2.3, it shall be a priority of the trustee to ensure and maintain proper housing for the Decedent. The trustee is to have discretion to invest principal or accumulated income in appropriate housing, subject to the restrictions set forth by court order. The trustee is encouraged to invest in property in whatsoever form as will maintain the Decedent in a home-like environment. Homestead or home-like environment shall not include nursing homes or institutions of any facility which would be financed by government entitlements, but for the investment made under the terms of Trust.

Additionally, the trustee is to allocate funds to be used in order to provide modifications which would make the home more accessible and comfortable for a person with a disability. There shall be no invasion restrictions with regard to housing modifications. The trustee shall have sole discretion with regard to determining the reasonableness of a financial allocation for a housing modification without court approval.

Under Article 3.2, the trustee has discretion to reimburse, from Trust income only, any member of the family or friend who needs payment for travel arrangements in order to visit with the Decedent, if the Decedent cannot travel to them for any reason whatsoever. It is the intent of the Settlor that Decedent's expenses be paid to permit him to travel to his family and friends when possible. It is Settlor's intent that the trustee be instructed to use funds to encourage family members to visit by providing reasonable reimbursement, if necessary, for payment of travel arrangements for this purpose.

Article 4.5 provides that upon the death of the Decedent, the trustee may pay expenses of the Decedent's last illness, not covered by governmental and/or private insurance programs and funeral, and all administrative expenses relating to Trust, including reasonable attorney's and accountant's fees if, in the trustee's

sole discretion, other satisfactory provisions have not been made for the payment of such expenses.

Article 4.5 further provides that State shall be reimbursed for medical assistance provided to the Decedent during his lifetime, as consistent with federal and state law. The remaining principal and accumulated income shall be distributed pursuant to the laws of State with regard to intestate distribution. If there are no intestate distributees, then the residue of Trust is to be distributed to a charitable organization that qualifies as such under section 501(c)(3) of the Internal Revenue Code. The trustee shall have the right to designate which qualifying charitable organization shall receive the funds.

At the time of Decedent's death, the value of Trust assets was \$z. Following Decedent's death, Department reported that the amount of medical assistance provided to Decedent during his lifetime totaled \$w, an amount greater than \$z. Therefore, in accordance with Article 4.5 of Trust, the Department requested that the balance of the Trust corpus, after payment of final expenses, be paid to Department as partial reimbursement for the medical assistance provided Decedent during his lifetime.

Trustee intends to sell the appreciated assets held in Trust's investment account and use the proceeds to reimburse the Department.

Discussion:

Section 1014(a) provides, in relevant part, that the basis of property in the hands of a person acquiring the property from a decedent shall, if not sold, exchanged, or otherwise disposed of before the decedent's death by such person, be the fair market value of the property at the date of decedent's death.

Section 1014(b)(9) provides that for purposes of § 1014(a), property is considered to have been acquired from or to have passed from the decedent if the property was acquired from the decedent by reason of death, form of ownership, or other conditions (including property acquired through the exercise or non-exercise of a power of appointment), and the property is required to be included in determining the value of the decedent's gross estate under chapter 11 of Subtitle B of the Internal Revenue Code. See also, section 1.1014-2(b)(1) of the Income Tax Regulations.

Section 1.1014-1(a) provides that the purpose of § 1014 is, in general, to provide a basis for property acquired from a decedent which is equal to the value placed upon the property for purposes of the Federal estate tax. Accordingly, the general rule is that the basis of property acquired from a decedent is the fair market value of such property at the date of the decedent's death, or, if the decedent's executor so elects, at the alternate valuation date as prescribed in § 2032. Property acquired from a decedent includes, principally, property acquired by bequest, devise, or inheritance, and, in the case of decedent's dying after December 31, 1953, property required to be included in determining the value of the gross estate under any provision of the Internal Revenue Code.

Section 2001(a) of the Internal Revenue Code imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2033 provides that the value of the gross estate includes the value of all property to the extent of the interest therein of the decedent at the time of his death.

Section 20.2033-1(a) of the Estate Tax Regulations provides that the gross estate of a decedent who was a citizen or resident of the United States at the time of his death includes under § 2033 the value of all property, whether real or personal, tangible or intangible and wherever situated, beneficially owned by the decedent at the time of his death.

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death, (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income from the property.

Section 20.2036-1(b)(1)(ii) provides that the use, possession, right to the income or other enjoyment of the transferred property is considered as having been retained by or reserved to the decedent to the extent that the use,

possession, right to income, or other enjoyment is to be applied toward the discharge of a legal obligation of the decedent, or otherwise for his pecuniary benefit.

The Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, § 13611(b), 107 Stat. 312, 624 (1993) at 42 U.S.C. § 1396p (d), (1994) provides for the establishment of supplemental needs trusts (SNTs), the corpus of which can be used for the benefit of a disabled person without jeopardizing his or her eligibility for government benefits. Under the statute, an SNT established for a beneficiary who is under age 65, with the beneficiary's own funds, is not treated as an "available resource" for purposes of determining Medicaid eligibility if the trust contains a "payback" provision providing that before any assets that remain in the trust at the death of disabled beneficiary can be distributed to any remainder beneficiaries of the trust, the State is required to be paid the amounts remaining in the trust up to the amount of all medical assistance paid on behalf of the beneficiary under a state plan. See, 42 U.S.C. §1396p (d)(4)(A).

Under 42 U.S.C. § 1396p (a)(1), a lien may be imposed against the property of the individual on account of medical assistance paid or to be paid on the individual's behalf under a state plan. For purposes of this section, the estate of the individual with respect to which a lien may be imposed includes: 1) all real and personal property and other assets included in the individual's estate, as defined for purposes of the applicable state law; and 2) may include, at the option of the state, any real and personal property and other assets in which the individual had any legal title or interest at the time of his death, including assets conveyed to a survivor, heir, or assign of the deceased individual through joint tenancy, tenancy in common, survivorship, life estate, living trust, or other arrangement.

State Statute 3 grants public welfare officials the right to bring an action against the estate of a decedent to recover the cost of public assistance or care provided such person.

In the present case, the funds contributed to Trust were awarded to the Decedent as compensation for Decedent's personal injuries and were contributed to the Trust by Decedent's guardian, acting on his behalf. Thus, for purposes of section 2036, Decedent was the transferor of the funds transferred to the Trust. Under the terms of the Trust, the trustee is required to expend trust

income and corpus exclusively for the Decedent's benefit during his lifetime pursuant to definite standards governing expenditure of income and invasion of corpus contained in the trust instrument. Further, on Decedent's death, the trustee is required to reimburse the appropriate State program for the costs of public assistance provided the Decedent. The Decedent's estate would otherwise be liable for these amounts. Accordingly, we conclude that the value of the Trust corpus on the date of Decedent's death is includible in the Decedent's gross estate under section 2036. Cf. Arrington v. United States, 108 F. 3d 1393 (1997). The amount paid by the Trust to Department as reimbursement for medical assistance provided to Decedent is deductible under § 2053(a)(2) (allowing an estate tax deduction for claims against the estate).

Further, the Trust assets held in Trust on the date of Decedent's death, that are includible in decedent's gross estate as discussed above, constitute property acquired from the Decedent by reason of Decedent's death, within the meaning of § 1014(b)(9). Therefore, the basis of the assets in the hands of the trustee of the Trust is the fair market value of the property at the date of Decedent's death (or alternate valuation date, if applicable).

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Except as specifically ruled herein, we express no opinion as to the consequences of this transaction under the cited provisions of the Code or under any other provisions of the Code.

This ruling is based on the facts and applicable law in effect on the date of this letter. If there is a change in material fact or law (local or federal) before the transactions considered in this ruling take effect, the ruling will have no force or effect. If the taxpayer is in doubt whether there has been a change in material fact or law, a request for reconsideration of this ruling should be submitted to this office.

Sincerely yours,

GEORGE MASNIK
Branch Chief, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special
Industries)

Enclosure

Copy of letter for section 6110 purposes

cc:

cc:

